BlackRock

April 14, 2021

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Re: Joint Statement Regarding Complex Financial Products and Retail Investors

BlackRock, Inc. (together with its affiliates, "**BlackRock**")[1] respectfully submits its comments to the Securities and Exchange Commission ("SEC" or "Commission") in response to the SEC's Joint Statement Regarding Complex Financial Products and Retail Investors.[2] As noted in the statement, retail investors have a wide array of investment options available to them and investors may not be aware of varying regulations depending on product structure and the unique risks posed by complex products. We believe retail participation in markets is positive for the entire ecosystem. However, clear and consistent disclosure and education is necessary in order to better protect investors and give them the tools they need to make informed investment choices, particularly regarding complex exchange-traded products.

Exchange-Traded Products

The exchange-traded product (ETP) market has grown substantially, with assets under management in US ETPs up from $70 billion in 2000 to $5.4 trillion as of December 31, 2020.[3] Along with this growth in assets, the US market has also experienced a growth in the number of ETPs available to investors, up from 95 to more than 2,600 over the same period.[4] As the number of ETPs has increased, so too has the number of more structurally complex products, including ETPs with different risk profiles and more narrowly tailored investment objectives. Examples of these products are exchange-traded notes (ETNs) and products that seek to provide a leveraged or inverse return of their benchmark.

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[1] BlackRock is one of the world's leading asset management firms. We manage assets on behalf of institutional and individual clients worldwide, across equity, fixed-income, liquidity, real estate, alternatives, and multi-asset strategies. Our client base includes pension plans, endowments, foundations, charities, official institutions, insurers, and other financial institutions, as well as individuals around the world.
[2] SEC, "Joint Statement Regarding Complex Financial Products and Retail Investors," October 28, 2020
[3] Source: Markit, BlackRock as of December 31, 2020
[4] Source: Markit, BlackRock as of December 31, 2020

Market events in 2020 underscored the importance of labeling these products in a manner that helps investors better understand the very different risks and considerations posed by increasingly complex ETPs.[5] While all ETPs share certain characteristics, including exchange-tradability, "ETF" has become a blanket term to describe products with a wide range of structures and features (and, in some instances, where the products in question are not "funds" at all).[6] As such, we believe that an ETP classification system would not only benefit investors by setting clear expectations about the inherent risks of different types of ETPs, but also assist regulators in developing appropriate regulations and help brokerage platforms systematically implement point-of-sale safeguards.

In May 2020, BlackRock, Inc., as part of a coalition including Charles Schwab Investment Management, Inc., Fidelity Investments, Invesco Ltd., State Street Global Advisors and The Vanguard Group, submitted letters to the New York Stock Exchange (NYSE), Nasdaq and Cboe Global Markets (Cboe) requesting the exchanges' support in implementing an ETP classification system. Specifically, the group suggested that certain ETPs with complex structures and/or certain embedded risks should be identified and categorized by the exchanges at the data feed level (via exchange listing rules or otherwise) as exchange-traded notes ("ETNs"), exchange-traded commodities ("ETCs") or exchange-traded instruments ("ETIs") rather than as ETFs (see Appendix for proposed categories and definitions).[7]

We believe that implementing an ETP classification system at the point of listing, as described above, would swiftly and effectively address many of the concerns raised by the Commission, including:

- Product classifications applied at the point of listing would flow "downstream" to data service providers (e.g., Bloomberg, Markit) and, ultimately, brokerage platforms. The ability to rely on a single, universally accepted classification system would allow brokerage platforms to systematically implement point-of-sale guardrails for self-directed investors, offering additional protection for retail investors outside of Regulation Best Interest.
- A classification system embedded as part of exchange listing rules would be uniformly applied across product structures. Rather than implement limits or requirements based on structure (such as use of leverage, as covered under the Investment Company Act, for example), such an approach would instead cohesively provide transparency to investors about the risks and structural features of complex products across multiple product structures.
- All investors, including advised and self-directed retail investors, would benefit from additional transparency into the risks and complexities of different ETPs to better manage expectations around product performance.

[5] See, for example, Akane Otani and Sebastian Pellejero, "'Bankrupt in Just Two Weeks'—Individual Investors Get Burned by Collapse of Complex Securities," The Wall Street Journal, June 1, 2020
[6] See, for example, Rachel Evans and Carolina Wilson, "The ETF's Wonky Cousin Can Trip Up a Sophisticated Investor," Bloomberg, February 4, 2019; and Simon Constable, "Could Some VIX-Related Funds Go Poof in a Day," The Wall Street Journal, September 4, 2017 (identifying an ETN as a "fund")
[7] See the letters submitted to NYSE, Nasdaq and Cboe, available at: https://www.blackrock.com/corporate/literature/publication/letters-to-exchanges-regarding-etp-crassification-051320.pdf

In our view, the proliferation of more structurally complex ETPs, including ETPs with different risk profiles and more narrowly tailored investment objectives, warrants a comprehensive ETP classification system to better inform investors' decisions.

Retail Investor Access to Markets

Recent market events have shown the increasing trend of retail investor participation in the markets. Broad retail participation in our public markets is positive for the entire ecosystem. Investing is an important building block for wealth creation, and market quality is improved through broadening and diversifying participation. As retail investing increases, it is important to provide retail investors with equitable access to markets and create a more level playing field with respect to information and market data. As such, developments which lower barriers to entry, make trading easier and more intuitive, and reduce the cost of investing benefit society by expanding equity ownership to a greater proportion of the population.

Specifically, new or inexperienced investors should be provided with the resources to help them understand market infrastructure, the attendant risks of trading on margin or using complex instruments with embedded leverage or options, their brokers' responsibilities and discretionary authority, and the impact of capitalization on a broker's level of service. In addition, with the emergence of new entrants and technical platforms in the broker dealer ecosystem, regulators should ensure that there is a minimum investor education standard which is being met and the suitability due diligence applied across brokers is consistent for investors who are accessing margin or complex instruments.

Moreover, as the use of social media becomes more prevalent, social media firms should work with regulators to protect investors from market manipulation and potentially fraudulent comments which could incite harmful behavior. Technology has dramatically transformed the manner through which information is disseminated and people interact. As such, regulators should take the steps needed to continue to have access to the data and tools necessary to protect investors and maintain fair and orderly markets.

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We appreciate the opportunity to comment and would welcome further discussion on the important topic of retail investor protection and education.

Sincerely,

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Kate Fulton
Managing Director, Head of US Public Policy

Appendix: Categories of Exchange-Traded Products

ETF	**Exchange-Traded Fund**	• A registered open-end management investment company under the Investment Company Act (operating under Rule 6c-11 or an applicable SEC ETF exemptive order) that: (i) in the normal course issues (and redeems) creation units to (and from) authorized participants in exchange for a basket and a cash balancing amount (if any); and (ii) issues shares that are listed on a national securities exchange and traded at market-determined prices; • Includes funds that transact on an in-kind basis, on a cash basis, or both; and • Excludes ETNs, ETCs and ETIs (as defined below).
ETN	**Exchange-Traded Note**	• A debt security issued by a corporate issuer (i.e., not issued by a pooled investment vehicle) that is linked to the performance of a market index and trades on a securities exchange; • May or may not be collateralized, but in either case, depends on the issuer's solvency to deliver fully to expectations; and • Excludes products that seek to provide a leveraged or inverse return, a return with caps on upside or downside performance or "knock-out" features.
ETC	**Exchange-Traded Commodity**	• A pooled investment vehicle with shares that trade on a securities exchange that invests primarily in assets other than securities and financial futures; • The primary investment objective of an ETC is exposure to traditional commodities and non-financial commodity futures contracts; and • May hold physical commodities (e.g., precious metals) or invest in non-financial commodity futures or commodity-based total return swaps.
ETI	**Exchange-Traded Instrument**	• Any pooled investment vehicle, debt security issued by a corporate issuer, or similar financial instrument that trades on a securities exchange that has embedded structural features designed to deliver a return other than the full unlevered positive return of the underlying index or exposure (for example, products that seek to provide a leveraged or inverse return, a return with caps on upside or downside performance or "knock-out" features); or • All products not captured by the ETF, ETN or ETC classification fall under ETI.